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TAGS: ECON EFIN PGOV RP
SUBJECT: Philippine GDP Growing Rapidly, But Challenges Remain

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Summary

¶1. Philippine Gross Domestic Product grew 7.5% year-on-year during the second quarter, a twenty-year high. Government spending helped spur the expansion. Economists now expect full-year economic growth at the upper end of the government's 6.1%-6.7% target range. Sustaining higher growth will require higher levels of private sector investment, which are dependent on implementation of reforms to make the economy more open and competitive and the investment regime more welcoming. End Summary.

GDP Growth Exceeds Expectations

¶2. According to the Philippine National Statistical Coordination Board, second-quarter Gross Domestic Product grew 7.5% year-on-year. That expansion represented a twenty-year high, beat the 6.5% consensus forecast, and outpaced the growth registered by most Asian neighbors (with the exception of Singapore and China). (Like most developing countries, the Philippines reports year-on-year rather than seasonally-adjusted annualized growth rates. GRP statisticians estimate the seasonally-adjusted annualized growth rate at between 6.8%-7.1%.) With growth estimated at 7.1% during the first quarter, cumulative first half growth was 7.3% year-on-year. First half Gross National Product (which includes the remittances of overseas Filipino workers) increased by 8% in real terms from the first semester of 2006.

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Expenditure Accounts: Striking Growth in GRP Spending
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¶3. On the demand side, personal consumption grew 6.0%, government consumption grew 11.8%, and capital formation grew 9.3%; all above first half 2006 growth of 5.4%, 5.3%, and 0.9%, respectively. These more than offset a deceleration in the growth of exports from 17.2% to 16.8%.

¶4. While personal consumption continued to fuel the economy's expansion on the demand side (helped by workers remittances), the acceleration in government consumption and construction expenditures during the first six months of the year was striking. This reflected a deliberate effort to boost non-debt spending after the passage of new tax measures, with election-related spending for the May 2007 congressional and local polls providing additional impetus during the period.

¶5. Government construction spending grew nearly 34% during the first half of 2007; a second consecutive year of growth after declines that saw government construction spending drop by over 60% between 2000 and 2005. The combination of expansion of public sector consumption and infrastructure expenditures produced nearly 20% of the total year-on-year growth in aggregate demand during the first half of 2007, up from just 7.6% in 2006.

¶6. Private construction investments grew 8.5%, boosted in part by migrant workers' investments in real estate, the demand for office space from the business process outsourcing industry, and lower interest rates. Investments in durable equipment rose a modest 2% year-on-year during the first half of 2007.

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Production Accounts: Services and Industry Lead
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¶7. Services output grew 8.6% and industry grew 7.2%, both rates higher than in the first half of 2006 (6.2% and 4.9%, respectively). These sectors more than made up for the slower expansion of agricultural output (which was hit by unfavorable weather conditions).

¶8. Transportation/communications increased 10.1%, (fueled in part by promotional activities and the robust expansion of cellular, fixed line, and broadband services) and spurred most of the acceleration in service sector growth.

¶9. The faster expansion of industrial sector output mainly reflected more construction activity (up 20.6% year-on-year). Mining/quarrying grew 24.3%, up from barely 3% the previous year.

Comment

¶10. Macroeconomic stability, the result of important and politically difficult fiscal reforms undertaken in 2005, have provided a foundation for growth, while the resulting revenues have been used to spur growth via increased infrastructure investments. As important as those investments are, they will not be sufficient to keep Philippine growth rates up with those of their neighbors in the long term. To bring about sustained growth at levels which would bring down poverty, the government will need to implement economic and political reforms, including privatization, liberalization of investment and trade regimes and a more effective judicial system. Readers may wish to refer to the listing of Embassy economic objectives in these areas on the Philippines Economic Priorities page of the Intellipedia on the classified network at www.intelink.sgov/wiki/Philippines_Economic_P riorities.

Kenney